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Director-Federal Regulatory
Southwestern Bell Corporation
1401 I Street, N.W., Suite 1100
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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Dear Bill:

Re: RM-8388, Southwestern Bell Telephone Company's
Comments to MFS' Inquiry into Policies and
Programs to Assure Universal Telephone Service in
a Competitive Market Environment.

Enclosed please find an original and five (5) copies of the above-referenced pleading to be filed with the Secretary of the Commission on Thursday, December 16, 1993. Also enclosed is a copy of the pleading to be file-stamped and returned to me.

Additional copies of the pleading are attached to be used as the courtesy copies and one is included for your files.

Bill, please hold the pleading until 1 p.m. EST and then file it with the Commission. Please call to confirm that the pleading has been filed. Thank you for your assistance.

Very truly yours,

One Bell Center
Room 3520
St. Louis, Missouri 63101

Enclosure

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BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
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DEC 16 1993

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of)

Inquiry into Policies and Programs to)
Assure Universal Telephone Service in a)
Competitive Market Environment)

RM-8388

TO: The Commission

COMMENTS OF
SOUTHWESTERN BELL TELEPHONE COMPANY

SOUTHWESTERN BELL TELEPHONE COMPANY

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December 16, 1993

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SUMMARY*

SWBT agrees that universal service issues raised in MFS' Petition for NOI warrant Commission attention, but strenuously objects to MFS' ploy of suggesting that there is a need to conduct a universal service proceeding before issuing the NPRM on access charge reform that USTA and many others have shown to be imperative. MFS' position is an embarrassingly transparent attempt to delay much-needed access reform simply to prolong the competitive advantages it currently enjoys over LECs due to outdated, asymmetric regulations.

The Commission can issue the access reform NPRM sought by USTA without any concerns over potential ill effects upon universal service. Nothing in access reform contradicts what needs to be done in a universal service proceeding. In fact, access reform complements universal service because it includes a public policy structure which identifies discrete public policy elements for price management purposes. If felt necessary, the Commission could always conduct separate access reform and universal service proceedings, but MFS has presented absolutely no justification for delaying essential access charge reform until after a universal service proceeding. Indeed, access reform can and should be effected by the end of 1994, no matter what the Commission may decide to do in the area of universal service.

A specific approach is required for addressing universal service issues properly. The appropriate framework for such an

* Abbreviations in the Summary are referenced within the text.

evaluation is straightforward: Given a competitive environment, what are the appropriate means for maintaining universal service? Also, specific support issues would need to be addressed, such as the need for an equitable and competitively neutral funding base, a neutral third-party administrator of the support program, and appropriate transitional mechanisms for LEC support.

Further, continuing LEC carrier-of-last-resort obligations would need to be addressed in a pro-competitive manner. LEC readiness-to-serve obligations which require up-front investment with no hope of recovery must be avoided.

MFS attributes to LECs the claim that a contribution to local service is provided whenever the price of a LEC's service exceeds its economic costs. However, the point that the Commission should bear in mind is that upward pressure on certain LEC rates, including local exchange service, will result from lost LEC contribution, regardless of what specific proportions of the contribution losses were used to recover local access costs as opposed to other LEC costs (such as overhead costs).

MFS' blatant attempt to stall the federal access charge reform that is critical for LECs to compete evenly with CAPs and others, and thereby benefit consumers and the public interest, should be seen for what it is and be summarily rejected by the Commission.

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of

Inquiry into Policies and Programs to
Assure Universal Telephone Service in a
Competitive Market Environment

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RM-8388

TO: The Commission

COMMENTS OF
SOUTHWESTERN BELL TELEPHONE COMPANY

Southwestern Bell Telephone Company (SWBT), by its attorneys, respectfully submits these Comments regarding a Petition for a Notice of Inquiry and En Banc Hearing (Petition) filed on November 1, 1993 by MFS Communications Company, Inc. (MFS). SWBT agrees with MFS that certain universal service issues raised in its Petition warrant attention by the Commission.

However, SWBT strenuously objects to MFS' disingenuous ploy of suggesting that there is a need to conduct a universal service inquiry proceeding (and, presumably, a subsequent universal service rulemaking proceeding as well) before even issuing the notice of proposed rulemaking on access reform that the record already shows is needed by the industry without further delay. This position is simply yet another baseless, transparent attempt by MFS to delay being subjected to competition from local exchange carriers (LECs) on the merits.

I. INTRODUCTION

Apparently, upon realizing that the United States Telephone Association (USTA) September 17, 1993 Petition for

Rulemaking (USTA Petition) on access charge reform bears great merit and may be favorably acted upon by the Commission, MFS decided that it needed to do something to delay that process. Without such delay, MFS runs the risk that the Commission might promptly modify the current access charge plan, as urged by USTA, so that LECs would be able to compete with MFS on more even terms.

Thus, coincidentally, on the same day that comments were due on USTA's Petition (November 1, 1993), MFS filed its Petition for a Notice of Inquiry on universal service issues, which might more accurately have been captioned "Petition To Delay Access Reform." SWBT does not dispute that Universal Service issues deserve Commission attention, but there is simply no reason to delay the access charge reform needed now by the industry in order to first address universal service issues.

II. UNIVERSAL SERVICE ISSUES SHOULD BE ADDRESSED IN A SEPARATE PROCEEDING CONDUCTED AFTER OR OVERLAPPING THE USTA ACCESS REFORM NPRM PROCEEDING.

SWBT agrees with the need for a comprehensive evaluation of universal service issues. However, SWBT strongly disagrees with MFS' suggestions that this review take place prior to access reform efforts that are now underway. MFS suggests that "it would be desirable to conduct the [universal service] hearing and inquiry promptly, before actions are taken in other dockets that may have major substantive impacts on universal service" (p. 3), and more directly states that "universal service issues should be considered separately from, and in the early stages, of any overall review of access charges" (p. 7).

SWBT agrees that the issue of universal service should be evaluated separately from other proceedings because of its broad considerations. However, SWBT does not share MFS' desire that access reform be put on hold while the Commission forges a path through the critical and extremely complicated issues surrounding universal service. The USTA proposal for access reform provides a framework for regulation in an environment of ever-increasing competition. It does nothing to harm universal service goals. In fact, one of the objectives of USTA's proposal is to promote universal service. The proposal recommends the creation of a public policy basket for rate elements which provide support for the Commission's universal service objectives while permitting LECs to compete effectively for services in competitive market areas. Moreover, as SWBT and others have demonstrated, the need for access reform is immediate and is paramount to a more fully competitive environment. Given the Commission's intent to facilitate additional competition as evidenced in the switched access and special access collocation proceedings, the public interest dictates that access reform be completed in 1994.

For some time, major industry participants have been investigating interstate access reform and a majority of them are in agreement that access reform should be addressed immediately. For example, Ameritech and Rochester Telephone Company each have filed petitions which proposed changes to the interstate access charge plan. NARUC filed a selection of alternatives to interstate access reform as an attachment to its Petition for NOI. Recently, the Commission's Common Carrier Bureau released its white paper on

interstate access reform. Further, the Commission now has before it the USTA Petition which represents an exhaustive investigation and a feasible plan for resolution of the issues surrounding the interstate access charge plan.

The entire industry, including end users, interexchange carriers (IXCs), LECs, consumer advocacy groups, state regulators and competitive access providers (CAPs) have been afforded the opportunity to participate in discussions regarding the results of these investigations. Representatives from each of these industry groups, including MFS, have developed positions and provided comments.

It would be most unrealistic for anyone to believe that a sufficient record does not exist for the Commission to proceed with an aggressive effort to reform the interstate access charge plan without delay. In view of the record developed in the aforementioned proceedings, the Commission can easily conclude that the access marketplace has changed sufficiently to warrant reform of the governing rules and regulations. Otherwise, the public interest will not be served.

SWBT believes the answer to MFS' concern is simple. The Commission should initiate a proceeding on universal service shortly after an NPRM on access reform based on the USTA proposal. By doing so, the Commission can alleviate MFS' concern "that resolution of critical policy issues concerning universal service should not await the outcome of a lengthy access charge reform docket" (p. 8). Both access reform and universal service are

fundamental issues facing the Commission today, and each can be addressed in dockets that overlap one another in time.

SWBT agrees with MFS that the assurance of universal service is "one of the Commission's most significant public service responsibilities" (p. 2), and that it is important for the Commission to maintain the leadership role on universal service (p. 8). The most appropriate way to satisfy these responsibilities is to initiate a proceeding on universal service issues without delaying other, equally important proceedings such as access reform.

No matter how long a universal service proceeding may take, access charge reform as sought by USTA can and should be effected no later than 1994. It is expected that the Commission's Price Cap reform will be completed during 1994, and it is clear that there are some important interrelationships between that effort and the needed access charge reform. There is no reason why both of those proceedings cannot or should not be conducted concurrently and both be completed by the end of 1994.

III. A SPECIFIC APPROACH IS NECESSARY TO ADDRESS UNIVERSAL SERVICE ISSUES PROPERLY.

A. Framework For Evaluation

MFS suggests that there are two fundamental aspects to universal service policy that must be addressed:

- 1) What financial support/subsidy mechanisms are appropriate?
- 2) How should the funds needed for these programs be raised?
(p. 7)

SWBT agrees that these are very important issues that must be addressed. The proper framework for examining universal service issues will be a key to determining the changes that are required. SWBT suggests that the proper framework for this evaluation be based upon the question: Given a competitive environment, what are the appropriate means for maintaining universal service? Once a clear policy direction on universal service is established, then more specific issues can be resolved.

Resolution of these issues will clearly consume a great deal of time. The Commission cannot hold all other issues in abeyance while answering these fundamental issues regarding universal service. This does not mean that discussion of the specifics need be avoided while developing the guiding policies and principles. To the contrary, it merely suggests that the industry should not prejudice answers to these specific issues without addressing the much broader aspect of what universal service is to be and how it is to be accomplished in the new environment of competition and merging industries.

B. The Concept of Universal Service

MFS' reference to the Communications Act of 1934 (p. 2) forms the basis of the concept for universal service. The industry's current ability to serve all communities and customers (both high and low cost, urban and rural) has evolved through a number of implicit and explicit subsidies and support mechanisms. These mechanisms have helped provide financial support to achieve and sustain universally available, reliable telecommunications service at reasonable prices.

SWBT has identified some of the current interstate mechanisms which have helped make universal service a reality, and includes a list and description of those mechanisms within Attachment 1 to these Comments. These mechanisms fall into several general categories such as: (1) the Universal Service Fund; (2) Long Term Support; (3) Carrier Common Line (CCL); (4) \$25 Special Access Surcharge; (5) Social Policy Pricing; (6) Lifeline; (7) Linkup; (8) Telecommunications Relay Service (TRS) Fund; (9) Capital Recovery/Depreciation; and (10) Dial Equipment Minutes Weighting. Clearly, an analysis of these complex mechanisms will be very time consuming and intensive, and will also require the participation of state regulatory agencies.

Under the industry paradigm in place prior to the adoption of regulatory policies promoting increased competition, implicit and explicit support mechanisms adequately provided for accomplishment and maintenance of universal service goals. In the new competitive paradigm, however, the approach to universal service must change as the ability to recover costs for universal service is dramatically affected by competitive and regulatory forces. Among other things, pricing flexibility, rate deaveraging and, if necessary, explicit support to specific companies should be used to eliminate existing implicit support mechanisms.

C. Specific Support Issues Must Be Addressed In Any Universal Service Proceeding.

While SWBT does not claim that universal service by nature conflicts with the notion of local competition, it does believe that the methods currently employed to promote universal

service goals are not compatible with the proliferation of local competition. Methods such as averaged pricing, support flows between services, and uneconomic depreciation are not sustainable in an increasingly competitive environment. Regulatory decisions have facilitated a more competitive environment without modifying the methods by which universal service is to be maintained in that environment. MFS complains that "LECs reflexively invoke the phrase 'universal service' to discourage regulators from introducing increased local service competition" (p. 2). SWBT strongly disagrees with this unsubstantiated assertion. While SWBT and other LECs have raised universal service concerns, these concerns have been founded upon the fundamental problems caused by introducing widespread asymmetric competition while failing to modify the methods for achieving universal service established during an era of limited competition.

For example, one of these methods includes the implicit support that flows between services and geographic areas. The Commission staff paper recognizes that implicit support flows exist. MFS in its Petition also recognizes that this support flow exists (MFS, p. 10). While SWBT supports the concept that geographic areas "pay their own way," SWBT realizes that this will require rate increases in some areas. In fact, even MFS seems to realize this, although it glosses over the point in a footnote, saying that a "transition" is necessary "to avoid subjecting rural customers to rate shock" (p. 11, n. 13).

This is the very basis of the LECs' universal service "reflex." Of course, the LECs are not the only party to possess

this reflex. Congress exhibited the same concern with the Commission's earlier plans for full transition of Carrier Common Line (CCL) revenues to the Subscriber Line Charge (SLC).

Raising universal service concerns is not an attempt to discourage regulators from increasing competitive entry. To the contrary, it is an attempt to persuade regulators that issues associated with universal service must be addressed as a result of their decisions to actively promote competition. SWBT believes that the new competitive paradigm requires a new universal service paradigm (i.e., a change in the method of recovery.) The two, at present, are inherently inconsistent and are not mutually sustainable. SWBT hopes the resolution of universal service issues will help rectify these concerns and therefore fully supports the need to examine universal service issues, provided that essential access charge reform is not unreasonably delayed as a result.

1. An Equitable And Competitively Neutral Funding Base Will Be Necessary.

SWBT is pleased that MFS is willing to provide funding for the support mechanisms that may be necessary to promote universal service goals. This is one area where there seems to be general agreement among the interested parties.¹ SWBT supports the need for an equitable and competitively neutral funding base for any support mechanisms that may be required.

¹ See, for example, comments and reply comments on USTA's petition for rulemaking for access reform addressing universal service objectives and funding requirements. Commentors generally agreed that funding should be broad-based and should incorporate a competitively neutral method.

MFS proposes a "play or pay" system where a single "Universal Service Assurance" (USA) fund would be created to collect and distribute financial support for universal service goals.² SWBT supports the "concept" of one fund for collection and distribution of explicit support funding requirements. The funding requirements for the explicit support mechanism should not be finalized until the appropriate regulatory freedoms for pricing flexibility and rate deaveraging have been provided to the LECs. This action should reduce the requirements for explicit funding. Pricing flexibility and rate deaveraging should include both provisions for rate increases and decreases in order to recover costs incurred by the LECs. The resulting reasonable prices would have to be further evaluated to determine if specific customer support would be required to make service available at affordable prices. Targeting of support must be directed to achieve different objectives, but a "USA" fund could be used to collect and distribute the money necessary for any future support mechanisms that may be required and for current programs such as Lifeline/Linkup, the Universal Service Fund (USF) and the Telecommunications Relay Support (TRS) program.

2. The Administrator Of A Support Program Should Be A Neutral Third Party.

In discussing its proposal for future support funding mechanisms, MFS suggests that a disinterested third-party

² MFS, pp. 18-21 and Attachment 1. While not an important issue at this point, this fund could be labeled the "Universal Service Preservation" (USP) fund to avoid confusion from use of the acronym "USA."

administrator be designated for managing the support fund. SWBT agrees with MFS that a third party should administer any explicit support program, but disagrees with MFS that the National Exchange Carrier Association (NECA) should be excluded from consideration. None of the duties listed by MFS are beyond the capabilities of NECA to perform. In addition, the network necessary to collect and distribute the support is also in place and currently administered by NECA. Since NECA and, presumably, any such third party would only be acting as an agent for the Commission, which would retain the final responsibility, the degree of authority provided to NECA or any other third party would determine the ability of the administrator to avoid becoming bogged down in recurring and acrimonious disputes.

3. Transitional Mechanisms For Support To LECs Will Be Necessary.

MFS raises a number of support or "subsidy" issues throughout its Petition. For example, it complains about "alleged 'implicit' or 'hidden' subsidies that supposedly make possible universal, affordable local exchange service" (p. 2), and that it is "open to question" whether a "blanket subsidy of 'high-cost' LECs" is warranted any longer" (pp. 10-11). MFS further asserts that there are "perverse incentives in the existing system, which rewards LECs for having high costs" (p. 11). MFS also alleges that "LECs obviously have every incentive to inflate the apparent amount of subsidy to delay and frustrate the evolution of a competitive market" (p. 14).

Although some of MFS' allegations are clearly unfounded, other issues raised by MFS warrant consideration. For example, SWBT supports the position that a competitive marketplace requires the reevaluation of the existing methods for implementing universal service. MFS, however, does not seem to want to acknowledge the past decisions that were made to support public policy objectives. These past decisions are now inconsistent with the competitive future of telecommunications. To rectify the situation, the industry and regulators must recognize that the past social contract must be substantially revised to ensure a fair and equitable transition.

SWBT fundamentally agrees with MFS that particular services should not be subsidized (p. 10), and that "rural areas should, as a general proposition, pay their own way for telephone service" (p. 11). However, it is doubtful that such industry changes will be implemented overnight. It will be necessary to develop transitional funding methods as the industry progresses to a more fully competitive marketplace. In fact, MFS recognizes this need, although it glances over the problem as if it were minor (p. 11, n. 13). MFS observes in a footnote that transitional changes would have to be phased in over some period of time; however, it does not provide any detail on how it proposes this process to unfold. SWBT suggests that dealing with these transitional methods will be a difficult and complicated, but highly necessary task to ensure that significantly increased competition does not hamper the maintenance of universal service.

There are a number of transition mechanisms that have been employed in the past. These include the transition over an eight-year period for the existing USF (Rule 36.641), the transition from a combined allocation factor to the dial equipment minute (DEM) [Rule 36.125(c) - (e)], and the transition from the subscriber plant factor (SPF) to a 25% gross allocator for non-traffic sensitive plant [Rule 36.154(d)]. Any one of these approaches could provide a reasonable mechanism once the starting point and end points were defined. The important part of the process is to establish the starting point by first providing appropriate pricing flexibility and rate deaveraging in order to minimize the extent of explicit support required to both companies and targeted customers.³

In an apparent effort to discredit the need for continued support to LECs, MFS argues that excessive subsidies are harmful in two ways. First, it suggests that subsidies "create economic inefficiencies by stimulating usage of some services (those that receive subsidies) and discouraging usage of other services (those that provide the subsidies)" (p. 13). SWBT agrees. That is why SWBT and others have argued for replacing implicit support that is prevalent in today's pricing levels with explicit support or by adjusting prices to more appropriate levels.⁴ MFS believes that subsidy programs should initially be limited to POTs access (MFS,

³ Separations and depreciation reform are also potential means by which to minimize the extent of such explicit support. Such rate deaveraging would also respond to MFS' stated concern over alleged barriers to competitive entry in rural areas (p. 12).

⁴ See September 17, 1993 USTA Petition for Rulemaking, pp. 14, 20-45; SWBT's November 16, 1993 Reply Comments, pp. 22-23.

p. 10). With regard to subsidy levels, MFS states that "[s]ome level of 'inefficiency' must be tolerated, and indeed may even be desirable, to assure that the telephone network remains a ubiquitous national asset" (MFS, p. 13). However, MFS questions the level of contribution identified in the Monson Rohlfs Study (MFS p. 13).

A ubiquitous national asset requires that a LEC provide not only POTs access facilities, but also facilities that provide connectivity between all areas, including those served by other LECs, and a reasonable means of access for other telecommunications service providers. Past and current regulation has promoted inefficient pricing schemes, such as geographic rate averaging, in the interest of achieving universal service goals. The Monson Rohlfs Study estimated large amounts of potential net revenue flow or contribution (included in LEC prices) that may be impacted by competition.⁵ This amount was derived by estimating the difference in prices that LECs currently charge for toll and access services

⁵ See, p. 18 and n. 7, infra. Whether this contribution flow is used to support basic local exchange service alone or used to support a "ubiquitous national asset," is subject to service-specific cost definitions on which there is significant disagreement. For instance, MFS claims that loop costs are joint and common, while LEC studies support that such costs are attributable to, and caused by decisions to access a LEC's network. An extensive discussion of why local loop costs are not joint and common appears in Alfred Kahn and William Shew, "Current Issues in Telecommunications Regulation; Pricing," Yale Journal on Regulation (Spring 1987), pp. 191-256. Also see, Alfred E. Kahn, "Pricing of Telecommunications Services; A Comment," Review of Industrial Organization (vol. 8, 1993), pp. 39-47; William Taylor, "Efficient Pricing of Telecommunications Services: The State of the Debate," Review of Industrial Organization (vol. 8, 1993), pp. 21-37; and Lester Taylor, "Pricing of Telecommunications Services: Comment on Gabel and Kennet," Review of Industrial Organization (vol. 8, 1993), pp. 15-19.

and their respective long-run incremental costs. Obviously, in a competitive marketplace, inefficient pricing will not be allowed to continue and such contribution is at risk. A new regulatory construct is necessary; otherwise, universal service and the ubiquitous national asset that MFS refers to is at risk.

Second, MFS states that subsidies "create uneconomic incentives for users to avoid those services whose prices are inflated by subsidy funding requirements" (p. 13). SWBT also agrees with this point, which is why support funding requirements should not be tied to specific services. Rather, any required funding for support mechanisms should be based on a competitively-neutral, equitable method. SWBT also recognizes that support to suppliers will be necessary over some period of time to ensure the equitable reconciliation of the past social contract for implementing universal service goals. SWBT supports the elimination of inappropriate subsidies; however, that process will require substantial regulatory change.

D. MFS' Position on Local Exchange Service Is Unclear.

MFS asserts that "[c]ompetition in local telephone service need not result in increases in basic local rates" (Attachment 1); however, its position is somewhat confusing. It is unclear whether MFS supports the continuance of support to basic services or whether MFS supports the concept of allowing prices for basic services to more accurately reflect costs. In its Attachment 1, MFS first indicates that services should not be subsidized and that rural customers should pay their fair share. Later on in the same attachment (whose pages are unnumbered), MFS suggests that

providers of "subsidized" service would receive credits for serving eligible consumers but only after "rates would be allowed to move to cost-based levels." However, in the section of this attachment alleging that basic rates do not have to increase, MFS appears to be suggesting that a competitively-neutral fund be established to continue the support-based pricing for basic services.

These varied positions are unclear and seem to be only a ploy to (1) limit support to LECs for maintaining universal service, and (2) convince regulators that increased competition will not result in the need to increase the price of "basic" service for certain consumers. SWBT supports the concept that implicit support between services should not be required. But it is absurd to suggest that "basic" service rates will be unaffected by the withdrawal of such support. That is not consistent with the reality of a competitive marketplace.

E. Continuing LEC Carrier-Of-Last-Resort Obligations Must Be Addressed In A Pro-Competitive Manner.

MFS indicates that

[t]o further assure universal service, the incumbent monopoly LECs should continue for the foreseeable future (until alternative services are widely available) to be required to serve all customers within their existing service areas (although they would receive a Universal Service Assurance Fund credit for serving eligible consumers at subsidized rates). Since rates would be allowed to move to cost-based levels (before Universal Service Assurance credits), however, LECs would be fully compensated for serving all customers and there would be an economic incentive for CAPs and other carriers to compete to serve these customers, even in 'high-cost' areas, if they can do so more efficiently (Attachment 1; emphasis added).

SWBT certainly supports the concept that LECs should be allowed to adjust rates to better recover costs. SWBT also recognizes that it alone, over the near term, is the only carrier capable of providing services to all areas it now serves.⁶ However, certain issues must be dealt with concerning obligation to serve and carrier-of-last-resort requirements in a transitionally competitive marketplace. For example, carrying such requirements may imply "readiness-to-serve" obligations which may require up-front investment with little or no hope of recovering that investment if competitors eventually win the customer. These types of issues must be dealt with to ensure that such obligations do not carry competitive penalties for LECs.

F. As Contribution Used To Recover LEC Overhead Costs Declines, LECs will Ultimately Raise Prices Of Other Services.

MFS claims that "LEC studies assume that a 'contribution' to local service is provided whenever the price of a service exceeds its 'economic cost'" (p. 15). While the particular study MFS refers to at this point is not clear, an earlier reference is made to a study which concludes that large LEC contribution levels might be associated with markets currently experiencing competitive

⁶ SWBT does not support "[t]he 'big myth' that universal service inherently requires that local service be provided by subsidized and protected monopolies" (MFS, p. ii). It is clear that evolving technologies allow alternatives to traditional local service. SWBT welcomes competitive alternatives provided it is allowed to be a full competitor on even terms.

entry.⁷ The point of this study is that if LEC prices are not adjusted as competition in selected markets intensifies, then the contribution earned by LECs in these markets is subject to severe erosion. As contribution used to recover LEC costs declines, LECs will ultimately raise prices of other services, including local exchange service, in an attempt to recover total operating costs (including the cost of capital).⁸ The upward pressure on certain LEC service prices will result from lost contribution, regardless of what specific proportions of the contribution losses were used to recover local access costs as opposed to other LEC costs (such as overhead costs).

MFS also states that LEC prices might exceed the costs of providing service as a result of incorrect calculations of cost, inappropriate allocations of overhead costs, inefficient LEC operations, or abnormally high returns on capital investment (p. 16). If the true costs of providing carrier access services are lower than current LEC prices, then competitive entry should produce declining LEC prices. However, it is not likely that MFS is urging the Commission to lower LEC carrier access charges. Alternatively, if LECs are earning relatively high profits in the carrier access market, yet overall company earnings do not exceed prescribed levels, then the revenues earned from LEC sales of carrier access services is contributing to the recovery of other LEC operating costs.

⁷ MFS, p. 13, n. 15. The study referenced is Calvin S. Monson and Jeffery H. Rohlf, "The \$20 Billion Impact of Local Competition in Telecommunications," Strategic Policy Research (July 16, 1993).

⁸ Monson and Rohlf, p. 3.

If regulatory practices produce LEC rates that are well above costs in a specific market, potential entrants (such as MFS) will find that market and the prevailing LEC prices particularly appealing. Alternatively, where prevailing LEC prices produce little, if any, contribution toward LEC overhead costs, potential entrants will find little allure in those markets. A number of firms have entered the carrier access market, yet few if any are actively competing with LECs in the provision of local loops to widely dispersed residences. A primary reason for this is perhaps the current LEC price/cost differentials prevailing in the carrier access and local loop markets. MFS' claims that LEC carrier access prices are not recovering any of the costs of providing local loops is aimed more at preventing LEC carrier access rate reductions than at avoiding local rate increases. Indeed, if MFS' claim that current LEC rate structures are "separate from universal service policy concerns" (pp. 14-15) is actually true, then MFS and state and federal regulators should be indifferent between current LEC prices and a set of rates which exhibit significantly lower carrier access charges and substantially higher local service prices. SWBT seriously doubts, however, that either MFS or regulators (especially state commissions) would, in fact, be indifferent in their reactions to these different scenarios.


IV. CONCLUSION

The universal service issues raised by MFS can and should be addressed by the Commission. However, other than financially aiding CAPs by perpetuating the competitive asymmetries of the current federal access charge rules, there is no benefit whatsoever in delaying the needed access charge reform merely to address universal service issues first. Both areas could be addressed in separate proceedings that overlap in time. However, for the public interest to be served, the Commission should conduct and conclude the USTA access charge reform proceeding no later than year-end 1994.

Respectfully submitted,

SOUTHWESTERN BELL TELEPHONE COMPANY

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